89-271

No. _____

IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM 1989

RAY J. BELISLE, et al.,[1]

Petitioners,

vs.

RALPH C. ANZIVINO, Trustee
of the bankruptcy estate of
Oliver Plunkett and Monica Plunkett,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

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QUESTION PRESENTED

May the trustee in a bankruptcy case use 11 U.S.C. §544(a)(3) to bring into the estate property that the debtor holds in constructive trust for his fraud victims, in spite of the restrictions of §§541 and 550?

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[1] The other petitioners are PAN-AM PAVILION-I, a partnership, PAN-AM PAVILION-II, a partnership, PAN-AM PAVILION-I, a partnership, PAN-AM PAVILION II, a partnership, PAN-AM COMPANY, a partnership, PHILIP R. BELISLE, PETER BELSKY, ROSEMARY BELSKY, JANE BURTON, LYNN E. BURTON, ROBERT J. CORBETT, BETTY CORBETT,

GILBERT J. COUILLARD, JR., DOROTHY M. COUILLARD, JOHN R. DUNN, MARGOT R. DUNN, PETER L. EISENMANN, JOSEPHINE G. EISENMANN, RICHARD P. EISENMANN, MELINDA S. EISENMANN, CHARLOTTE FALK, SANDS G. FALK, EUNICE FRIDL, BRIAN FRIDL, LAWRENCE N. FRIDL, FREDERICK J. GALLES, BURZOE K. GHANDHI, NANCY GHANDHI, JERRY L. GILBERT, LYNN P. GILBERT, DONALD D. HILLAN, CAROLYN B. HILLAN, RONALD C. JOHNSON, MORRIS KATZ, HELEN KELLENBERG, JACK KELLING, JEANNE KELLING, ANTHONY A. KLEINHEINZ, SHIRLEY KLEINHEINZ, VIRGINIA KLEINHEINZ, DONALD C. LOZIER, MICHAEL J. MARINELLE, SAMUEL R. MCCREADIE, THOMAS O. MIOTKE, DONNA MIOTKE, DANIEL MOSCA, MARY LOU MOSCA, PATRICK K. PLUNKETT, MARIE PLUNKETT, EDWARD F. POPEK, ALICE POPEK, RUGENE E. RAY, MILDRED W. RAY, ADELINE M. REWOLINSKI, CHARLES E. ROESSGER, ELIZABETH ROESSGER, EUGENE C. ROHLOFF, ROSEANN ROHLOFF, RICHARD J. ROSLAWSKI, TERESIA E. ROSLAWSKI, NORMAN O. SANDE, JOAN SANDE, STEPHAN P. SAZAMA, THOMAS R. SCHNEIDER, JANE SCHNEIDER, RUDOLPH J. SCRIMENTI, ROBERT A. SEITZ, VIOLETA A. SINGSON, RALPH SLOWIK, RUTH SLOWIK, EDWARD STAACKE, YVONNE STAACKE, HELEN STURGULEWSKI, SALOMEA STURGULEWSKI, JOHN A. TARNASKI, DONALD H. THIMM, STEPHEN T. VNUK, SHARON VNUK, RALPH J. ZIELINSKI, ROBERT F. ZIELINSKI, and MARY ZIELINSKI.

Oliver Plunkett and Monica Plunkett are listed as appellees in the court of appeals decision, but they have never participated in this case at any level.

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PETITION FOR A WRIT OF CERTIORARI
TO THE UNITED STATES COURT OF APPEALS
FOR THE SEVENTH CIRCUIT

The petitioners, Ray J. Belisle, et al., respectfully request that a writ of certiorari issue to review the opinion and judgment of the United States Court of Appeals for the Seventh Circuit entered on June 6, 1989.

OPINIONS BELOW

The memorandum decision of the United States Bankruptcy Court for the Eastern District of Wisconsin is reported as In re Plunkett, 89 B.R. 776 (Bankr. E.D. Wis. 1988). The United States District Court for the Eastern District of Wisconsin affirmed the bankruptcy court decision in an unreported opinion. The United States Court of Appeals for the Seventh Circuit affirmed the district court decision in an opinion

not yet reported but available at 1989 U.S. App. LEXIS 8682.

JURISDICTION

The judgment for which review is sought was entered by the United States Court of Appeals for the Seventh Circuit on June 6, 1989. The jurisdiction of this court rests on 28 U.S.C. §1254(1).

STATUTES INVOLVED

The following sections of Title 11, United States Code, are involved in this matter:

> §541 Property of the estate.
>
> (a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located:
>
> (1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

. . .

(3) Any interest in property that the trustee recovers under section 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

. . .

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

. . .

§544 Trustee as lien creditor and as successor to certain creditors and purchasers.

(a) The trustee shall have, as of the commencement of and case, and without regard to any knowledge of the trustee or of any creditor, the

rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by--

(1) a ... [judicial lien creditor];

(2) a[n] ... [execution creditor]; and

(3) a bona fide purchaser of real property from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser at the time of the commencement of the case, whether or not such a purchaser exists.

. . .

§550 Liability of transferee of avoided transfer.

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from--

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

. . .

§551 Automatic preservation of avoided transfer.

Any transfer avoided under section 522, 544, 545, 547, 548, 549, or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the estate but only with respect to property of the estate.

NOTE: The foregoing statutes are reproduced here as they existed prior to the enactment of Public Law No. 98-353, the Bankruptcy Amendments and Federal Judgeship Act of 1984, because §553(a) of said Act provides that the amendments it makes are effective as to cases filed 90 days after the date of enactment of said Act. The date of enactment was July 10, 1984, and the Plunkett case was filed in 1982.

STATEMENT OF THE CASE

During the spring and summer of 1979, Oliver Plunkett induced various parties to

invest in partnerships he was forming to purchase a 50-year leasehold interest in the Pan-Am Pavilion shopping center in Christiansted, St. Croix, Virgin Islands. After getting the cash, Plunkett purchased the leasehold interest, but he took title in his own name despite having used partnership funds for the purchase. He recorded the assgnment of lease in his own name, and he dealt with tenants and creditors as if he were the sole owner.

On the other hand, Plunkett dealt with the various partners as if they were all co-owners of the Pan-Am Pavilion with him. He frequently referred to the Pan-Am Pavilion as partnership property in correspondence with the other partners, and he recognized partnership ownership for tax purposes, listing it as partnership property on the federal and Wisconsin partner-

ship tax returns, and furnishing the partners with annual I.R.S. forms advising them of the partnership income and deductions they should report on their personal tax returns.

In 1982, Plunkett and his wife filed a bankruptcy petition in the United States Bankruptcy Court for the Eastern District of Wisconsin pursuant to Title 11 of the United States Code (the Bankruptcy Code). They listed among their assets a percentage interest in a Pan-Am Pavilion partnership, but they did not list the Pan-Am Pavilion leasehold as an asset.

As the court of appeals stated,

> Plunkett [had] bamboozled the partners and used for his own benefit the leasehold acquired with partnership funds. Virgin Islands law impresses a constructive trust on the leasehold and its fruits. A constructive trust ordinarily survives bankruptcy: the property may not be used to satisfy the debtor's obligations to other creditors.

Slip op. at 3. Accordingly, the other partners commenced an adversary proceeding

to quiet title to the leasehold property. The bankruptcy trustee claimed entitlement to the leasehold property as a "bona fide purchaser" under 11 U.S.C. §544(a)(3). The bankruptcy court granted the Trustee's motion for summary judgment, the district court affirmed under 28 U.S.C. §158(a), and the court of appeals affirmed under 28 U.S.C. §158(d).

REASONS FOR GRANTING THE WRIT

The decision of the Court of Appeals for the Seventh Circuit is inconsistent with pronouncements of this Court and of other courts of appeals. District courts and bankruptcy courts, relying on contrary analyses by different courts of appeals, reach inconsistent results, sometimes contradicting themselves from one page to the next. The unsettled law leaves bankruptcy

trustees and creditors in doubt as to their relative rights and obligations, spawning frequent and costly litigation.

Furthermore, the opinion of the court of appeals does not take into account certain statutory provisions that are inconsistent with its holding.

1. Inconsistency With Supreme Court Pronouncements

Section 544(a)(3) of the Bankruptcy Code invests a bankruptcy trustee, to some extent at least, with the status and attributes of a "bona fide purchaser of real property from the debtor." Thus for example, the trustee qua bona fide purchaser could defeat the interest of a prior transferee of real estate from the debtor if that transferee had neglected to record his instrument of title.

In this case, the court of appeals

held that §544(a)(3) allows the Trustee to defeat the interests of the petitioners even though there was no prior transferee, and even though the property in question was held by the debtor in constructive trust for the benefit of the partners whose money he had used to purchase the property. Since the debtor held the property in constructive trust, all he had was bare legal title, and this Court has previously stated that

> Congress intended to exclude from the estate property of others in which the debtor had some minor interest such as a lien or bare legal title.

U.S. v. Whiting Pools, Inc., 462 U.S. 198, 204, n. 8 (1983).

Furthermore, this Court has also stated that "Congress plainly excluded [from the bankruptcy estate] property of others held by the debtor in trust at the time of the filing of the petition." Id.

at 205, n. 10.

Thus, the court of appeals has allowed the Trustee to use §544(a)(3) to bring into the estate property this Court has found to be "plainly excluded" by Congress.

2. Split of Authority Among Circuits

While §544(a)(3) permits a trustee to bring certain property into a bankruptcy estate, §541(d) excludes from the bankruptcy estate certain equitable interests in property. Some courts have held that §541(d) prevails over §544(a)(3), others have held just the opposite, others have noted a conflict without resolving it, and still others have found that there is no conflict.

The Fifth Circuit has decided that §541(d) prevails over §544(a)(3). In

Georgia Pacific Corp. v. Sigma Service Corp., 712 F.2d 962, 968 (5th Cir. 1983), the court interpreted §541(d) to require a trustee to turn over the constructive trust res to the beneficiaries, stating,

> If indeed all or part of the money so owed was subject to a constructive trust ..., the bankruptcy court would be required to recognize those equitable interests and, perhaps, the debtor in possession's [i.e., trustee's] sole permissible administrative act thereto would be to pay over or endorse the sums due to the beneficial owners of the property.

This line of reasoning was followed in In re Quality Holstein Leasing, 752 F.2d 1009, 1013 (5th Cir. 1985), in which the court discussed the interaction of §§541 and 544, concluding that

> As a general rule, it must be held that section 541(d) prevails over the trustee's strong-arm powers. Although those powers allow a trustee to assert rights that the debtor itself could not claim to property, Congress did not mean to authorize a bankruptcy estate to benefit from property that the debtor did not own.

This conclusion was reiterated by the court in In re Emerald Oil Co., 807 F.2d

1234, 1238 (5th Cir. 1987), which quoted the foregoing language from Quality Holstein Leasing in its entirety. Although the court of appeals below dismissed this conclusion as "dictum," slip op. at 8, Quality Holstein Leasing has been followed by various lower courts, both within and without the Fifth Circuit, and by the Eighth Circuit.

In In re Earl Roggenbuck Farms, Inc., 51 B.R. 913, 917 (Bankr. E.D. Mich. 1985), the court, which is in the Sixth Circuit, cited Georgia Pacific and Quality Holstein Leasing in concluding that, under §541(d), "if a creditor holds an equitable interest in property, the trustee may not avoid that interest by resorting to §544(a)." To the same effect is In re Atlantic Mortgage Corp., 69 B.R. 321, 330 (Bankr. E.D. Mich. 1987), which relies on Quality

Holstein Leasing and In re Flight Transp. Corp. Securities Litigation, 730 F.2d 1128 (8th Cir. 1984), cert. den. sub nom. Reavis & McGrath v. Antinore, 469 U.S. 1207 (1985).

In Flight Transp. Corp. Securities, 730 F.2d at 1136, the Eighth Circuit stated that

> where, under state law, the debtor's fraud or other wrongful conduct gives rise to a constructive trust, so that the debtor holds only bare legal title to the property, subject to a duty to reconvey it to the rightful owner, the estate will generally hold the property subject to the same restrictions.

Although the court did not discuss §541(d) vis-à-vis §544(a)(3), the court did conclude, in a later case, that "imposition of a constructive trust under state law upon a debtor's property generally confers on the true owner of the property an equitable interest in the property superior to

the trustee's ...." In re N.S. Garrott & Sons, 772 F.2d 462, 467 (8th Cir. 1985), citing Quality Holstein Leasing, Georgia Pacific, and Flight Transp. Corp. Securities.

The Third Circuit has taken the opposite point of view. In In re Elin, 20 B.R. 1012, 1016 (D.N.J. 1982), aff'd mem., 707 F.2d 1400 (3d Cir. 1983), the court held that

> assets recoverable by a trustee pursuant to § 544 become property of the estate notwithstanding the provisions of § 541(d). In other words, if a person other than the debtor holds an equitable interest in assets subject to recovery under § 544, the provisions of § 541(d) upon which plaintiff relies do not prevent the trustee from recovering those assets.

This, of course, is precisely the opposite of the holdings of the Fifth Circuit cases, and Elin has been followed by various lower courts outside the Third Circuit. For example, in In re Anderson,

30 B.R. 995, 1010 (M.D. Tenn. 1983), the court, which is in the Sixth Circuit, quoted extensively from Elin and stated that it "concurs completely" with the Elin court's interpretation of §§541(d) and 544.

The Ninth Circuit also concurs with Elin, although not necessarily completely. The court stated that the appellant's

> contention that under section 541(d) all beneficial or equitable owners of property may exempt their property from the debtor's estate in all circumstances, notwithstanding the debtor's legal title and the avoidance powers of section 544, goes too far. ... On the other hand, it is not necessary for us to go as far as the BAP [bankruptcy appellate panel], which held that section 541(d) applies only to those beneficial owners whose interests cannot be otherwise avoided under section 544. A fair reading of the statutes in this context mandates only that section 544(a)(3) prevail in this and similar instances.

In re Tleel, 876 F.2d 769, 773 (9th Cir. 1989) (emphasis in original). Thus, the Ninth Circuit has apparently held that

§544(a)(3) prevails over §541(d) sometimes, but sometimes not.

Other courts have found it unnecessary to decide whether or not §541(d) in fact prevails over §544 because the resolution of the particular case would be the same either way. In In re General Coffee Corp., 64 B.R. 702, 708 (S.D. Fla. 1986), the district court held that "§ 541(d) prevails over § 544 strong-arm powers" as a general rule. On appeal, the Eleventh Circuit observed:

> The drafters of the Bankruptcy Code appear not to have anticipated the potential for tension between sections 541(d) and 544(a). Since the enactment of § 541(d), however, many courts have recognized that these sections are not always easily reconciled because § 541(d) excludes certain equitable interests from the estate of a bankrupt while § 544(a) permits the trustee to bring certain tainted property into the control of the estate.

In re General Coffee Corp., 828 F.2d 699, 704 (11th Cir. 1987).

The court noted that some courts have held that "§ 541(d) prevails over the trustee's strong-arm powers under § 544(a)," while other courts have held that "property not part of the estate under § 541(d) may come into the estate under § 544(a)." The court then stated: "This circuit has never resolved the tension between sections 541(d) and 544(a). Nor do we need to do so here. The result in this case is the same under either approach." 828 F.2d at 705. Similarly, the Sixth Circuit has declined to resolve the apparent conflict between these two sections, finding that the case before it could be decided by reference to state law. In re Crabtree, 871 F.2d 36 (6th Cir. 1989).

The Seventh Circuit has sided with those courts allowing property excluded

from the estate by §541(d) to be brought into the estate by §544(a). The court stated:

> Section 541(d) does not have anything to say about the effects of §544(a)(3). It forbids including property in the debtor's estate "under subsection (a) of this section" and does not address whether property may be included under some other part of the Code. The courts that have perceived a conflict between §§541(d) and 544(a)(3) did not discuss this limitation on the domain of §541(d).

Slip op. at 7. The court perceived no conflict with the holding of any other court of appeals, but did concede that tension exists between its approach and opinions of other circuits.

This tension has resulted in courts across the country reaching disharmonious and contradictory results at all levels of the federal court system. Bankruptcy courts and district courts in circuits that have not ruled on this question are

left to choose between inconsistent precedent as they see fit, and they reach contradictory results. Only this court can put an end to the uncertainty that has resulted from apparently contradictory statutory language.

3. Statutory Construction: §544(a) vs. §541(d)

According to the court of appeals below,

> Section 541(d) does not have anything to say about the effects of §544(a)(3). It forbids including property in the debtor's estate "under subsection (a) of this section" and does not address whether property may be included under some other part of the Code. The courts that have perceived a conflict between §§541(d) and 544(a)(3) did not discuss this limitation on the domain of §541(d).

Slip op. at 7. However, what the court overlooks is that the debtor's estate as defined in §541(a) includes property acquired under §544(a)(3).

Therefore, to the extent §541(d) is a limitation on §541(a), it is ipso facto a limitation on §544(a)(3), so the "limitation on the domain of §541(d)" perceived by the court is illusory.

Section 541(d) "forbids including property in the debtor's estate 'under subsection (a) of this section.'" Slip op. at 7. Subsection (a) is intended to be an "all-embracing definition" of property of the estate. 124 Cong. Rec. H11,096 (daily ed. Sept. 28, 1978), [App. 3] Collier on Bankruptcy X1-101; 124 Cong. Rec. S17,413 (daily ed. Oct. 6, 1978), [App. 3] Collier on Bankruptcy X-27. Property of the estate under said §541(a), includes:

> (1) ... all legal or equitable interests of the debtor in property as of the commencement of the case.
>
> (3) Any interest in property that the trustee recovers under section ... 550 ....

> (4) Any interest in property preserved for the benefit of the estate ... under section ... 551 ....

Section 550 permits a trustee to recover property (or its value) from a transferee of a transfer avoided under §544. Section 541(a)(3) brings this property into the estate.

Section 551 preserves for the benefit of the estate any transfer avoided under §544. Section 541(a)(4) brings any property so preserved into the estate.

Thus, the estate created by §541(a) includes the "property that the trustee recovers under the avoiding powers." H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 368 (1977), reprinted in [App 2] Collier on Bankruptcy (15th ed. 1984). Consequently, to the extent §541(d) limits §541(a), it has to limit §544 as well, for §544 is incorporated within §541(a).

Although the court of appeals below did not recognize the statutory interrelationship of §§541 and 544, various other courts have, although not all have concurred with the foregoing conclusion that §541(d) limits §544(a)(3) when it limits §541(a). For example, in In re Elin, 20 B.R. 1012, 1016 (D.N.J. 1982), aff'd mem., 707 F.2d 1400 (3d Cir. 1983), the court recognized that "§ 541, and § 551 which is incorporated therein by reference, bring within the debtor's estate property recoverable pursuant to § 544." However, the court still held that §541(d) did not preclude recovery under §544. Similarly, the court of appeals below concluded that "reading the law [§541(d)] as limited to inclusions in the estate under §541(a) makes legal as well as linguistic sense," slip op. at 8, but

neither court explained how §541(d) can limit inclusions under §541(a) but not under §544(a) when inclusions under §544(a) are a subset of inclusions under §541(a).

4. Statutory Construction: The Transfer Requirement

Since property acquired by a trustee under §544 is brought into the estate by §541(a), and since this is done by means of §550 or §551, a pre-petition transfer of property of the debtor has to occur before a trustee can acquire property or avoid an interest under §544(a)(3). Both §550 and §551 by their terms apply to "transfers," so unless a "transfer" occurred, neither section would come into play, and, therefore, §§541(a)(3) and 541(a)(4) would not operate to bring into the estate property recovered under §544.

Section 550(a) provides that

> to the extent that a transfer is avoided under section 544 ..., the trustee may recover, for the benefit of the estate, the property transferred ... from ... the initial transferee of such transfer ... or ... any immediate or mediate transferee of such initial transferee.

Section 551 provides that any "transfer avoided under section ... 544 ... is preserved for the benefit of the estate." The court of appeals did not address these sections in concluding that "the statute mentions 'transfer' only in the sense of the hypothetical transfer that measures the trustee's rights." Slip op. at 7 (emphasis in original).

Furthermore, the court of appeals did not address the significance of the word "transfer" in §544(a)(3). That section refers to a "bona fide purchaser of real property from the debtor, against whom

applicable law permits such transfer to be perfected." (Emphasis added.) Presumably, if there is no transfer of real estate of the debtor, the phrase regarding the perfection of "such transfer" would be rendered meaningless. However, if the phrase is not meaningless, it may operate to limit the trustee's status as a bona fide purchaser, for if the statute gives the trustee the status of a bona fide purchaser who can be perfected against, his status may not operate as against a party who cannot perfect his interest (such as a constructive trust beneficiary), but the court of appeals did not address this question either.

CONCLUSION

The opinion of the court of appeals appears to be inconsistent with statements

of this Court and of other courts of appeals. The diversity of judicial pronouncements in this area has engendered confusion and costly litigation. In addition, the court of appeals appears to have ignored various provisions of the statutes in reaching its conclusions. For these reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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Dated: August 4, 1989

APPENDIX

In the

United States Court of Appeals

For the Seventh Circuit

No. 88-3189

RAY J. BELISLE, *et al.*,

Plaintiffs-Appellants,

v.

OLIVER PLUNKETT, MONICA PLUNKETT, and RALPH C. ANZIVINO, Trustee,

Defendants-Appellees.

Appeal from the United States District Court
for the Eastern District of Wisconsin.
No. 88-C-655—**Myron L. Gordon,** *Judge.*

ARGUED APRIL 3, 1989—DECIDED JUNE 6, 1989

Before BAUER, *Chief Judge*, and CUMMINGS and EASTERBROOK, *Circuit Judges.*

EASTERBROOK, *Circuit Judge.* May the trustee in a bankruptcy case bring into the estate property that the debtor holds in constructive trust for victims of fraud? Oliver Plunkett organized partnerships that provided funds to buy a 50-year leasehold interest in a shopping center, Pan-Am Pavilion in Christiansted, St. Croix, Virgin Islands. Plunkett treated the leasehold as his own—including making a collateral assignment to secure a loan of $100,000 that Plunkett put to personal use. Invoking the strong-arm powers of 11 U.S.C. §544, the Trustee claimed the

status of a bona fide purchaser for value. Both the bankruptcy court, 89 B.R. 776 (Bankr. E.D. Wis. 1988), and the district court held that §544(a)(3) allows the Trustee to claim the leasehold for the estate, leaving the partners to participate as creditors. The partners contend that §541(d) keeps the leasehold out of the estate and that the Trustee may not employ §544(a) to fetch into the estate something that §541(d) excludes.

Stripped of irrelevant detail, the facts are that in March 1979 Plunkett (a real estate entrepreneur operating out of Milwaukee) signed a contract, in his own name, to buy the leasehold from W.O.F. Associates for $1.2 million. Through the spring and summer of 1979 Plunkett formed five partnerships to raise the money for the acquisition. After getting the cash, Plunkett closed the deal in October 1979—in his own name, despite using partnership funds. He recorded the assignment of the leasehold in the St. Croix real estate records, again in his own name. Although Plunkett recognized the partnerships for tax purposes—he reported a share between 5% and 7%—and informed the partners of the income and deductions they should report on their own returns, he dealt with tenants and creditors as if he owned the leasehold.

Plunkett and his wife filed petitions under the Bankruptcy Code in 1982. After the Trustee asserted that the leasehold is an asset of the estate, the partners filed an adversary proceeding, seeking to quiet title in the partnerships. Chief Judge Clevert of the bankruptcy court granted the Trustee's motion for summary judgment, and the district judge affirmed on appeal under 28 U.S.C. §158(a). We have jurisdiction under §158(d) because the decision is the "final" disposition of an adversary proceeding that would be a stand-alone suit outside of bankruptcy. *In re Sandy Ridge Oil Co.*, 807 F.2d 1332 (7th Cir. 1986); *In re Morse Electric Co.*, 805 F.2d 262 (7th Cir. 1986). The partners have filed adversary proceedings against the Trustee personally, contesting his allocation of tax benefits (and detriments) from the leasehold during the administration of the estate, but as these were not consolidated with the quiet

title action, they do not affect appellate jurisdiction even though there is some overlap between the actions. Compare *Sandwiches, Inc. v. Wendy's International, Inc.*, 822 F.2d 707, 710 (7th Cir. 1987), with *In re Berke*, 837 F.2d 293 (7th Cir. 1988).

Plunkett bamboozled the partners and used for his own benefit the leasehold acquired with partnership funds. Virgin Islands law impresses a constructive trust on the leasehold and its fruits. A constructive trust ordinarily survives bankruptcy: the property may not be used to satisfy the debtor's obligations to other creditors, and the debts to the victims of the fraud may not be discharged. 11 U.S.C. §523(a)(2), (4). See *United States v. Whiting Pools, Inc.*, 462 U.S. 198, 204-05 nn. 8, 10 (1983); *In re Teltronics, Ltd.*, 649 F.2d 1236, 1239 (7th Cir. 1981). The Trustee acknowledges all of this but relies on §544(a)(3):

> The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—. . .
>
> > (3) a bona fide purchaser of real property from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser at the time of the commencement of the case, whether or not such a purchaser exists.[1]

[1] The text we have quoted is the original version of §544(a)(3), in force at the time the Plunketts filed their petition. An amendment in 1984 changed it to read: "a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such purchaser exists." The parties do not contend that this change makes a difference.

A bona fide purchaser of the leasehold interest, without notice of the earlier claim, would take ahead of a person who has not recorded his entitlement. Not only Virgin Islands real estate law, 28 V.I. Code §124, but also the Uniform Partnership Act, adopted in both the Virgin Islands and Wisconsin, 26 V.I. Code §42, Wis. Stat. §178.07(3), provides this. See also *In re Marino*, 813 F.2d 1562, 1565 (9th Cir. 1987) (trustee may avoid undisclosed partnership claim against real property under similar California statute). So the Trustee submits that the Plunkett estate includes the Pan-Am leasehold, "as of the commencement of the case", without need for action on his part.[2]

Not so fast!, the partners rejoin. The estate can't contain the leasehold "as of the commencement of the case" because §541(d) says that it does not contain property in which the debtor holds bare legal title:

> Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by

[2] The Virgin Islands has a race-notice rule, and constructive notice on the part of the purchaser would allow the holder of the unrecorded interest to prevail. Although §544(a) specifies that the trustee shall be treated as a person without *actual* notice, if any purchaser from the debtor would have had *constructive* notice of the claim—that is, would have been charged with realizing the implications of the obvious, even though they did not set off alarms at the time—then the trustee loses. See *McConnor v. Marston*, 679 F.2d 13, 16-17 (3d Cir. 1982). Virgin Islands law charges buyers with constructive notice of what they would have learned from examining the real estate records and interrogating persons in possession. Although the partners contend that any purchaser from Plunkett would have had constructive notice of their ownership, the bankruptcy and district courts held that the record did not create a genuine issue of material fact on that score. Plunkett dealt with the tenants in his own name or that of a proprietorship, so interrogating the tenants would not have disclosed the partnerships' interest. And looking in the real estate records would have been fruitless: Plunkett appeared as the sole owner.

> the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.[3]

If this were not enough, the partners continue, §544(a)(3) speaks of a "transfer", yet Plunkett did not transfer the Pan-Am leasehold, and there is therefore nothing for the Trustee to avoid. As the partners see things, §§ 541(d) and 544(a)(3) allow a trustee to recover property transferred out of the estate before the filing, but not to claim for the estate property held in a constructive trust. Several courts have perceived a "conflict" between §541(d) and §544(a)(3). E.g., *In re General Coffee Corp.*, 828 F.2d 699, 704-06 (11th Cir. 1987); *In re Quality Holstein Leasing*, 752 F.2d 1009, 1013-14 (5th Cir. 1985). The parties ask us to decide which statute prevails. We believe, however, that there is no conflict.

Section 544(a)(3) pulls into the debtor's estate property that ostensibly was there all along. Dealing with ostensible ownership is not, however, the statute's objective—at least not its only one—because the benefits are not limited to those who relied on the asset in extending credit. Section 544(a)(3) complements §§ 544(a)(1) and (2), which give the trustee the status of a judgment creditor vis-à-vis chattels in the debtor's possession. If one creditor had (or could get) a judgment effective against the chattels, the trustee secures the same advantage for all—which reduces any creditor's incentive to try to be first in line, a rush that may reduce the value of the debtor's assets. Thomas H. Jackson, *The Logic and Limits of Bankruptcy Law* 70-79 (1986); cf. Douglas H. Baird, *Notice Filing*

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[3] Like §544(a)(3), this section changed in 1984. Congress substituted "under subsection (a)(1) or (2) of this section" for "under subsection (a) of this section". The change does not affect this case.

and the Problem of Ostensible Ownership, 12 J. Legal Studies 53 (1983). Sections 544(a)(1) and (2) follow state law, however, in giving the trustee no *greater* rights than the judgment creditor would have. If the debtor possesses a stolen diamond ring, the real owner's rights would trump those of a judgment creditor, and under the Code therefore would defeat the claims of all of the debtor's creditors. Whether or not we say that the debtor holds the ring in "constructive trust" for the owner is a detail. Under state law the owner's claims are paramount; the debtor could not defeat those rights by pledging or selling the ring, and the creditors in bankruptcy receive only what state law allows them. *Butner v. United States*, 440 U.S. 48 (1979). Under most states' laws, however, the buyer in good faith of *real* property can obtain a position superior to that of the rightful owner, if the owner neglected to record his interest in the filing system. Section 544(a)(3) gives the trustee the same sort of position.

A bona fide purchaser from Plunkett would have taken ahead of the partners under local law. They neglected to record the partnerships' interest, though recording is easy. (The partners could, and in retrospect should, have refused to invest funds except through an escrow agent, who would have held the cash until good title had been recorded in the partnerships' names.) One of Plunkett's creditors, extending $100,000 against a collateral assignment of the leasehold, actually obtained a position superior to that of the partners. The Trustee claimed the same position for the estate (meaning the creditors collectively, including the partners).

Nothing in the text or function of §544(a)(3) makes the force of this claim turn on whether Plunkett once owned the leasehold and then sold it to the partnerships (but failed to record their interest) or whether, instead, Plunkett acquired the leasehold through the partnerships. The sequence W.O.F. to Plunkett (perhaps with a bridge loan) to Pan-Am partnerships, with Plunkett retaining ostensible ownership, is identical in every respect to the sequence W.O.F. to Pan-Am partnerships to Plunkett, with

Plunkett obtaining ostensible ownership. Identical from the perspective of Plunkett, of the partners, and of Plunkett's (other) creditors—and identical from the perspective of §544(a)(3). Section 544(a)(3) allows the trustee to have a bona fide purchaser's rights *or* avoid a transfer, so a "transfer" by the debtor cannot be a necessary condition of the exercise of the strong-arm power. The statute mentions "transfer" only in the sense of the *hypothetical* transfer that measures the trustee's rights: if a hypothetical bona fide transferee from the debtor would come ahead of the "true" owner's rights, then the trustee takes ahead of the true owner.

Section 541(d) does not have anything to say about the effects of §544(a)(3). It forbids including property in the debtor's estate "under subsection (a) of this section" and does not address whether property may be included under some other part of the Code. The courts that have perceived a conflict between §§ 541(d) and 544(a)(3) did not discuss this limitation on the domain of §541(d). Moreover, even if we confine attention to the estate defined by §541(a), §541(d) carves out only "an equitable interest in such property that the debtor does not hold." This could mean, as the partners treat it, "an equitable *interest* . . . that the debtor does not hold" (here, because subject to constructive trust), but perhaps the statute addresses "*property* that the debtor does not hold", on which, therefore, lenders were unlikely to rely in extending credit. If read to exclude any "equitable interest . . . that the debtor does not hold", the statute would remove from the estate even the Plunketts' house, if it had been mortgaged to secure a loan. Estates commonly include such property.

Section 541(d) was designed, its text and history reveal, to deal with persons with title to property who had sold the equitable interests. E.g., S. Rep. 95-989, 95th Cong., 2d Sess. 83-84 (1978). This is a common arrangement in secondary mortgage markets: a person with many titles sells certificates representing shares in the pool of income generated by the notes. Section 541(d) ensures that the creditors of the service corporation stand in line behind

the owners of the income stream. The bankruptcy court thought that because the legislative history speaks only of secondary mortgage markets, §541(d) is limited to such cases. 89 B.R. at 782-83. Legislative history does not carry so much force. Mortgage markets may have been the impetus for §541(d), but statutes often create rules that reach beyond the immediate concerns that spawned them. "It is not the law that a statute can have no effects which are not explicitly mentioned in its legislative history". *Pittston Coal Group v. Sebben*, 109 S. Ct. 414, 420-21 (1988). Section 541(d)'s genesis helps us understand, however, that reading the law as limited to inclusions in the estate under §541(a) makes legal as well as linguistic sense. See *In re Auto-Train Corp.*, 810 F.2d 270, 273 (D.C. Cir. 1987).

Although our reading of §541(d) and §544(a)(3) does not conflict with the holding of any other court of appeals, there is some tension between the course we believe appropriate and statements in other opinions. The Fifth Circuit said in *Quality Holstein Leasing*, 752 F.2d at 1013 (note omitted) that "[a]s a general rule, it must be held that section 541(d) prevails over the trustee's strong-arm powers. . . . Congress did not mean to authorize a bankruptcy estate to benefit from property that the debtor did not own." With all respect to the Fifth Circuit, we believe that allowing the estate to "benefit from property that the debtor did not own" is exactly what the strong-arm powers are about: they give the trustee the status of a bona fide purchaser for value, so that the estate contains interests to which the debtor lacked good title. The estate gets what the debtor could *convey* under local law rather than only what the debtor *owned* under local law—a critical distinction that the Fifth Circuit did not mention. The discussion of §541(d) in *Quality Holstein Leasing* is dictum, however, because the court held that state law did not impress a constructive trust on the property, and the trustee prevailed under §544(a)(3).

The Eleventh Circuit took a course opposite to that of the Fifth. It said in *General Coffee*, 828 F.2d at 704, "that

§544(a) would bring the [constructive] trust property into the estate in spite of §541(d)." But having proclaimed the supremacy of the strong-arm power, the court retreated to neutrality, 828 F.2d at 705-06, and then held that a bona fide purchaser for value would not have defeated the interest in question under state law. So in *Quality Holstein Leasing*, which proclaimed the supremacy of §541(d), the trustee won, and in *General Coffee*, which treated §544(a) as the victor, the trustee lost. For the reasons already canvassed, we believe that both the Fifth and Eleventh Circuits got off on the wrong foot by finding a "conflict" in need of resolution.

Section 544(a)(3) gives the Trustee the status of a bona fide purchaser for value. The bankruptcy and district courts reached the same conclusion. The partners' remaining contentions were waived or are insubstantial, so the judgment is

AFFIRMED.

A true Copy:

Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF WISCONSIN

In the Matter of:

OLIVER PLUNKETT
MONICA PLUNKETT,

Debtor.

RAY J. BELISLE, et al.,

Plaintiffs and Appellants,

v.

OLIVER PLUNKETT and
MONICA PLUNKETT,

No. 88-C-655

Defendants,

and RALPH C. ANZIVINO, TRUSTEE,

Defendant and Third-Party Plaintiff and Respondent

v.

PAN-AM PAVILION-I,
a partnership, et al.,

Third-Party Appellants,

JAMES RUTTER and
MARY RUTTER,

Third-Party Appellants.

DECISION and ORDER

This bankruptcy appeal stems from Chief Bankruptcy Judge Clevert's ruling that the trustee may invoke 11 U.S.C. § 544(a)(3) to avoid a constructive trust on the debtor's interest in certain real property located in the Virgin Islands. The issue before this court is essentially one of law which is reviewable de novo. See In re Duncan, 85 Bankr. 81, 82 (W.D. Wis. 1988). The decision will be affirmed.

In the bankruptcy court, the parties had filed cross motions for summary judgment and had stipulated to the issues of fact. Before the debtors, Oliver and Monica Plunkett, filed a chapter 11 bankruptcy petition and schedules in 1982, Mr. Plunkett purchased a shopping center in

the Virgin Islands, having raised the necessary capital from a number of investors. The investors were under the impression that limited partnerships would be formed and that the partnerships would purchase the property. The partnerships were not formed, and the only name on the record title of the property is that of Oliver Plunkett.

The appellants are the persons who provided the money that Mr. Plunkett used to purchase the property; the appellee is the bankruptcy trustee. Appellants' position is that the bankruptcy court should not have allowed the Virgin Island property to become a part of the bankruptcy estate via §§ 544(a)(3) and 550 of the bankruptcy code. They argue that § 544 (a)(3) is limited by § 541(d).

Section 541 provides:

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

...

(3) any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

...

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not the extent of any equitable interest in such property that debtor does not hold.

Section 550(a) provides:

Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b), or 724(a)

> of this title, the trustee may recover, for the benefit of the estate, the property transferred. ...
>
> Section 554(a)(3) provides:
>
> The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by-
> (a) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such purchaser exists.

Appellants suggest that this court interpret § 541(d) of the bankruptcy code as a limitation on § 544. The effect of this would be that only the legal title to the property, not the equitable interest, would become part of the debtor's estate; then, the appellants, as beneficiaries of

the constructive trust, would enjoy the benefits of the property to the exclusion of all the other unsecured creditors.

Chief Judge Clevert held that § 541(d) should be limited to secondary mortgage market transactions, and ruled that § 541(d) and § 544(a) operate independently. Before reaching these conclusions, Chief Judge Clevert examined the statute, its legislative history and the case law. I agree with Chief Judge Clevert's conclusion. This view promotes the bankruptcy code's goal of treating all unsecured creditors equally. Thus property not a part of the estate under § 541(d) may become part of the estate pursuant to §§ 544(a)(3) and 550. See In Re Great Plains Western Ranch Co., 38 B.R. 899 (Bankr. C.D. Cal. 1984). In re Cascade

Oil Co., 65 B.R. 35, 39 (Bankr. D. Kan. 1986) and In re Dlott, 43 B.R. 789 (Bankr. D. Mass. 1983).

The bankruptcy court was also correct in its application of the rule. Under § 544(a)(3), the trustee is given the status of a bona fide purchaser as of the date of the filing of the bankruptcy petition. The trustee may then bring into the estate any property that an actual bona fide purchaser would have been able to claim. In the case at bar, under Virgin Island law, the bankruptcy trustee in the cloak of a bona fide purchaser, would defeat the appellants' unrecorded interests. See V.I. Code Ann. title 28, § 124 (1975). I note that Chief Judge Clevert's decision to apply Virgin Island law is not disputed on this appeal.

Therefore IT IS ORDERED that the decision and order of the bankruptcy court dated June 16, 1988, be and hereby is affirmed.

Dated at Milwaukee, Wisconsin, this 31st day of October, 1988.

/s/ Myron L. Gordon
Senior U.S. District Judge

In the Matter of Oliver PLUNKETT
Monica Plunkett, Debtor.

Ray J. BELISLE, et al., Plaintiffs,

v.

Oliver PLUNKETT and Monica Plunkett,
Defendants.

and Ralph C. ANZIVINO, Trustee, Defendant
and Third-Party Plaintiff,

v.

PAN-AM PAVILION-I, a partnership, et al.,
Third-Party Defendants.

Bankruptcy No. 82-01119.

Adv. No. 82-1329

United States Bankruptcy Court,

E.D. Wisconsin.

June 16, 1988.

MEMORANDUM DECISION

C.N. CLEVERT, Chief Judge.

Plaintiffs filed this adversary on

October 12, 1982, seeking an order directing the trustee to execute and deliver to them an assignment and conveyance of a leasehold estate[1] (the "leasehold") in the United States Virgin Islands. The bases for their request were that the leasehold was partnership property rather than estate property or, alternatively, that Plunkett and later the trustee, held the leasehold subject to a constructive trust because Oliver Plunkett (Plunkett) acquired the property by fraud.

The trustee filed his answer and cross-complaint on November 22, 1982, and alleged that as of the petition date, Plunkett held legal title to the leasehold in his individual name and that plaintiffs' interests were avoidable pur-

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[1]The leasehold is more fully described as: Leasehold estate in No. 39 Strand Street, Town of Christiansted, St. Croix, U.S. Virgin Islands. Being the same Property subject to a ground

suant to 11 U.S.C. § 544(a)(3). On December 23, 1982, the trustee filed a third-party complaint, reiterating the assertion in his cross complaint, but naming additional parties in interest in response to the plaintiffs' defense that indispensable parties had not been joined.

The third-party defendants[2] answered on February 4, 1983, and counterclaimed

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lease dated April 21, 1965 from recorded in the Office of the Register of Deeds, St. Croix, U.S. Virgin Islands, Page 385, as amended by instrument of January 14, 1969 and as thereafter assigned by W.O.F. Corporation to W.O.F. Company by instrument dated April 30, 1970, both of which instruments were recorded as attachments to instrument No. 4589/79 recorded in the office of the Recorder of Deeds, St. Croix, on October 10, 1979 and as thereafter assigned by instrument dated October 1, 1979 by W.O.F. Associates to Oliver Plunkett, recorded in the Office of the Recorder of Deeds, St. Croix, U.S. Virgin Islands, on October 10, 1979 at filing No. 4586/79.

[2]For ease of discussion, the third-party defendants are hereinafter identified as plaintiffs.

requesting the Court to find that the balance due on a loan[3], received by Plunkett and secured by the leasehold and alleged partnership cash, may be set-off from any sums received by the trustee as a result of the continuing interests the trustee claims in the partnerships. This matter is now before the Court on cross motions for summary judgment supported by stipulated facts and supplemental affidavits.

FACTS

In 1965 W.O.F. Corporation acquired from Joseph Alexander a 50-year leasehold interest in the Pan-Am Pavilion-I ("Pan-Am"), a shopping center complex located in Christiansted, St. Croix, United States Virgin Islands.

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[3]The stated amount of principal and accrued interest due and owing as of December 31, 1981, was $181,446.

Subsequently, W.O.F. Corporation assigned its leasehold interest in Pan-Am to W.O.F. Associates. By an agreement dated March 2, 1979, W.O.F. sold its interest in Pan-Am to Plunkett for $1,200,000. (Stipulation, Exhibit 1.) On that date, fee title to Pan-Am was in David Lieberman and Chase Manhattan Bank, Trustees under the will of Joseph Alexander. This purchase contract named Plunkett as purchaser and did not refer to any other interests or persons as purchasers.

During the spring and summer of 1979, Plunkett and Michael Marinelle formed or attemped to form five partnerships which included in their respective names the terms "Pan-Am" or "Pan-Am Pavilion." Plunkett and Marinelle represented to interested parties that these partnerships

were formed to raise capital for the acquisition of the Pan-Am shopping center complex. Five different partnership agreements were executed, although Plunkett treated them as one. They had the same business address; they had the same federal employer's identification number; they filed a "consolidated" partnership tax return; and their partners received Schedule K-1 statements based on that return. Several of the partnership agreements purported to create limited partnerships. However, certificates of limited partnership were not filed in Wisconsin or the Virgin Islands. It also appears that from the time the Pan-Am leasehold was acquired through April 15, 1982, the date Plunkett filed his bankruptcy petition, none of the individual

partners resided in the Virgin Islands.

W.O.F. Associates conveyed its interest in Pan-Am to Plunkett on October 1, 1979. As part of that transaction Plunkett assumed W.O.F. Associates' $129,166.65 mortgage obligation to First Pennsylvania Bank, executed a mortgage note (Stipulation, Exhibit 2), and an $800,000.00 leasehold mortgage (Stipulation, Exhibit 3), in favor of W.O.F. Associates. Plunkett also tendered W.O.F. $261,495.76 cash, including a prior earnest money deposit of $50,000. At the closing, $211,495.76 was wire transferred to W.O.F. from an account in First Bank, N.A. in Milwaukee under the name of "Oliver Plunket & Associates". Some of the deposits to that account had come from the various members of the Pan-Am

partnerships.

An assignment of lease, conveying W.O.F. Associates' leasehold interest in Pan-Am, was also executed by W.O.F. Associates and Plunkett on that date. (Stipulation, Exhibit 4.) All these documents were executed by Plunkett without reference to any other person, interest or possible agency relationship.

The assignment of lease was recorded in the Office of the Recorder of Deeds, St. Croix, United States Virgin Islands, on October 10, 1979. The St. Croix office of Lawyers Title Insurance Corporation issued a policy of title insurance to Plunkett dated October 10, 1979, showing that the leasehold title to Pan-Am was vested in Plunkett individually. (Stipulation, Exhibit 5.)

By a letter dated October 2, 1979, First Pennsylvania Bank, N.A. was notified by W.O.F. Associates that it had sold its interest in Pan-Am to Plunkett. (Stipulation, Exhibit 6.) And on October 17, 1979, Plunkett's counsel informed the Estate of Joseph Alexander that W.O.F. Associates' interest in Pan-Am had been sold to Plunkett. (Stipulation, Exhibit 7.)

In correspondence with various members of the Pan-Am partnerships, Plunkett referred to Pan-Am as partnership property. However, in correspondence with tenants of Pan-Am, Plunkett referred to himself as the owner. (Response Brief in Support of Trustee's Cross-Motion for Summary Judgment, Exhibit A, Affidavit of Patricia A. Purtell, Exhibits A-8 to

A-24.) Federal and state tax returns filed by Plunkett listed Pan-Am as a partnership asset and reported rentals from and depreciation of Pan-Am as items of partnership income and deductions. Plunkett's personal property bankruptcy schedule, Schedule B-2, listed Plunkett as holding a partnership interest in a Pan-Am partnership. Other property schedules did not list Plunkett as holding a real property interest in Pan-Am.

The Schedule K-1 statements filed by Plunkett or the trustee as part of the Pan-Am partnership tax returns, listed Plunkett's interest in the Pan-Am partnerships' profits or losses during 1979 to 1983 as ranging from 5% to 6.84%. Plunkett's percentage interest in capital during 1979 to 1983 ranged from 0% to 2.04%.

On January 11, 1980 Plunkett executed a collateral assignment of lease in favor of First Pennsylvania Bank, N.A. as security for a $100,000 loan to Plunkett. (Stipulation, Exhibit 8.) This document specifically recites that Plunkett is the sole owner of the leasehold interest in Pan-Am and the sole owner of the landlord's interest in the leases to the Pan-Am tenants. The proceeds of this loan were used by Plunkett to make improvements to property unrelated to the Pan-Am partnerships. On January 21, 1980 the First Pennsylvania Bank recorded the collateral assignment in the Office of the Recorder of Deeds, St. Croix, United States Virgin Islands.

Between October 1, 1979 and April 15, 1982, the petition date, ten tenants exe-

cuted leases for space in the Pan-Am. (Stipulation, Exhibits 9-18.) The leases contain conflicting information regarding Plunkett's status. Some were executed by Plunkett as an individual and others were executed by him as a representative of Oliver Plunkett & Associates, a sole proprietorship owned by Plunkett. (Response Brief in Support of Trustee's Cross-Motion for Summary Judgment, Exhibit A, Affidavit of Patricia A. Purtell.) Leases executed by Plunkett did not consistently identify to whom and where rents were to be paid. The rents were payable to Plunkett (Stipulation, Exhibits 14-17), to Oliver Plunkett & Associates (Stipulation, Exhibits 12, 13, & 18), or to Pan-Am (Reply Brief in Support of Plaintiffs' Motion for Summary Judgment, Affidavits of

Anne Cartruccio and Maggie Collins), which was an account in Plunkett's name at First Pennsylvania Bank in Christiansted, St. Croix. (Response Brief in Support of Trustee's Cross-Motion for Summary Judgment, Exhibit B, Affidavit of Laurence P. Wielgos.)

On the petition date all tenants of Pan-Am occupied their premises pursuant to leases signed by Plunkett or his predecessor W.O.F. Associates and the record title to Pan-Am was as follows:

> Fee Title: David Lieberman and Chase Manhattan Bank, Trustees under the Will of Joseph Alexander
>
> Leasehold Title: Oliver Plunkett
>
> Mortgage and/or Security Encumbrances: a) Leasehold mortgage from Oliver Plunkett to W.O.F. Associates
>
> b) collateral assignment of lease from Oliver Plunkett to First Pennsylvania Bank, N.A.

DISCUSSION

The central issue presented in these cross-motions for summary judgment is whether 11 U.S.C. § 544(a)(3) permits Plunkett's Chapter 11 trustee to avoid a constructive trust[4] on his leasehold interest in the Pan-Am shopping center. Resolution of this issue is dependent on whether 11 U.S.C. § 541(d) limits a trustee's avoiding powers under § 544(a)(3). However,

> [t]he difficulty with a constructive trust theory is, of course, that the "trust" is neither a trust nor constructive, but is a device created by the court to prevent injustice. It has the effect in bankruptcy, if applied, of preferring one creditor over another on the basis of equitable principles. The same equitable principles, however, dictate that in bankruptcy all unsecured creditors be treated essentially alike.

D & F Petroleum v. Cascade Oil Company, Inc. (In re Cascade Oil Company, Inc.), 65

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[4] The trustee disputes the existence of a constructive trust, though for purposes of the summary judgment motions and this decision, it is

B.R. 35, 40 (Bankr. D.Kan.1986) (citations omitted).

Section 544(a)(3) cloaks a bankruptcy trustee with the status of a bona fide purchaser of real estate from the debtor as of the filing of the petition by providing:

> [t]he trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by ... a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

11 U.S.C. § 544(a)(3).

Successful use of the strong arm power allows a trustee to use § 550[5] or

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assumed to have existed prepetition.

[5]11 U.S.C. § 550 states in part:

§ 551[6] of the Bankruptcy Code to preserve or recover the affected property for the benefit of the bankruptcy estate. Here, however, the plaintiffs contend that § 544(a)(3) is unavailing because there was no transferee from whom the trustee can recover the property under § 550.

The plaintiffs have missed the mark. According to the majority view of constructive trusts, which appears to be followed in the Virgin Islands, a

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(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553(b) or 724(a) of this title, the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from--

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

[6] 11 U.S.C. § 551 states:

Any transfer avoided under section 522, 544, 545, 547, 548, 549 or 724(a) of this title, or any lien void under section 506(d) of this title, is preserved for the benefit of the

constructive trust arises when a party engages in conduct which would result in unjust enrichment.[7] Assuming that this equitable remedy is applicable to the case at bar, Plunkett held the Pan-Am leasehold in trust for the benefit of the plaintiffs because he used their money to purchase the property. This view is consistent with § 160 of Restatement of Restitution which states that: "[w]here a person holding title to property is subject to an equitable duty to convey it to another on the ground that he would be unjustly enriched if he were permitted to

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estate only with respect to property of the estate.

[7]There is an apparent split of authority as to when a constructive trust arises. The majority view holds that a constructive trust arises when the facts giving rise to fraud, undue influence, etc., occur. The minority view is that a constructive trust arises only at the time a court declares it to exist. See, Annotation, Imposition of a Constructive Trust in Property Bought with Stolen or Embezzled Funds, 38

retain it, a constructive trust arises."[8] Under the foregoing rule Plunkett would be duty bound to convey the leasehold to plaintiffs. In other words, Plunkett was under an obligation as constructive trustee to turn the leasehold over to the plaintiffs as trust beneficiaries.

Under § 544(a)(3) the trustee, as a hypothetical bona fide purchaser of real property, may avoid any obligation incurred by the debtor regardless of whether a transfer has occurred. In this case, Plunkett had an obligation to convey

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A.L.R.3d 1354, 1359 (1971); A. Scott, The Law of Trusts § 462.4 (3d ed. 1967); G. Gleason Bogert & G. Taylor Bogert, The Law of Trusts and Trustees § 472 (Rev. 2d ed. 1978). Both the Virgin Islands and Wisconsin appear to embrace the majority view. Francois v. Francois, 599 F.2d 1286 (3rd Cir. 1979); Wilharms v. Wilharms, 93 Wis.2d 671, 287 N.W.2d 779 (1980).

[8]The parties apparently agree that Virgin Islands law applies. Since there is no statute dealing with constructive trusts, the Restatement applies by virtue of V.I. Code Ann. tit. 1, § 4 (1967), which states:

the leasehold to the plaintiffs. This court is satisfied that that obligation may be avoided by the trustee under § 544(a)(3).

However, if, as the plaintiffs contend, a transfer is necessary for a trustee invoking § 544(a)(3), to recover property under § 550, the required transfer has occurred. Section 101(50)[9] defines transfer to include every mode of indirectly disposing of or parting with an interest in property. That being so, the actions which gave rise to the construc-

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The rules of the common law, as expressed in the restatements of the law approved by the American Law Institute, and to the extent not so expressed, as generally understood and applied in the United States, shall be the rules of decision in the courts of the Virgin Islands in cases to which they apply, in the absence of local laws to the contrary.

[9] 11 U.S.C. § 101(50) states:
"transfer" means every mode, direct or indirect, absolute or conditional, voluntary or involuntary, of disposing of or parting with property or with an interest in property, in-

tive trust effectuated a transfer by disposing of Plunkett's equitable interest in the leasehold. Therefore, even under the plaintiffs' construction of § 544, the trustee may avoid the interests of the plaintiffs in the leasehold and bring them into the estate under §§ 550 and 541 (a)(3).[10]

This brings us to the issue of whether §541(d)[11] is a general limitation

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cluding retention of title as a security interest and foreclosure of the debtor's equity of redemption;....

[10] 11 U.S.C. § 541(a)(3) states:

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

. . . . .

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 or this title.

[11] 11 U.S.C. § 541(d) states:

Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such

on a trustee's avoiding powers under § 544(a)(3). The plaintiffs argue that because Plunkett held the leasehold subject to a constructive trust, only the legal title to the leasehold and not the equitable interest is property of the estate. From this premise the plaintiffs conclude that the trustee is required to turnover the leasehold to them.

The plaintiffs also suggest a conflict between § 541(d) and § 544(a)(3) which prevents the trustee from invoking § 544(a)(3). This court disagrees with

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a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, become property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent of any equitable interest in such property that the debtor does not hold.

that conclusion. Where possible, perceived conflicts between related statutes should be reconciled in accordance with basic principles of statutory construction in order to give effect to all provisions of the statutes. 2A N. Singer, Sutherland Statutory Construction §§ 51.02 and 51.05 (Sands 4th ed. rev. 1984). This process begins by examining the language of the statute. Id. at § 47.01. However, in instances where statutory language is ambiguous, statutory interpretation usually continues by referring to legislative history. Id. at § 48.01.

Section 541(d) begins by reiterating what is already clearly stated in § 541(a), i.e., property of the estate includes bare legal interests held by a debtor as of the commencement of a bankruptcy case. It

then uses a secondary mortgage market example to help describe the circumstances where the statute would apply. Unfortunately this language is of limited value in determining the intended scope of the statute. Consequently, it was necessary to examine the statute's legislative history. According to Senate Report No. 989, regarding the Bankruptcy Reform Act of 1978, § 541(e), the forerunner of § 541(d), was designed to preserve the manner in which secondary mortgage market transactions were treated under the old Bankruptcy Act. The report states:

> Section 541(e) confirms the current status under the Bankruptcy Act of bona fide secondary mortgage market transactions as the purchase and sale of assets. Mortgages or interests in mortgages sold in the secondary market should not be considered as part of the debtor's estate. To permit the efficient servicing of mortgages or interests in mortgages the seller often retains the original mortgage notes and related documents, and

> the purchaser records under State recording statutes the purchaser's ownership of the mortgages or interest in mortgages purchased. Section 541(e) makes clear that the seller's retention of the mortgage documents and the purchaser's decision not to record do not impair the asset sale character of secondary mortgage market transactions. The committee notes that in secondary mortgage market transactions the parties may characterize their relationship as one of trust, agency, or independent contractor. The characterization adopted by the parties should not affect the statutes in bankruptcy of bona fide secondary mortgage market purchases and sales.

S. Rep. No. 989, 95th Cong., 2d Sess. 83-84 (1978), reprinted in 1978 U.S. Code Cong. & Admin. News 5787, 5869-70.

Remarks by Senator DeConcini reiterated this by stating:

> The purpose of section 541(d) as applied to the secondary mortgage market is identical to the purpose of section 541(e) of the Senate amendment and section 541(d) will accomplish the same result as would have been accomplished by section 541(e). Even if a mortgage seller retains for purposes of servicing legal title to mortgages or interest in mortgages

sold in the secondary mortgage market, the trustee would be required by section 541(d) to turn over the mortgages or interest in mortgages to the purchaser of those mortgages.

The seller of mortgages in the secondary mortgage market will often retain the original mortgage notes and related documents and the seller will not endorse the notes to reflect the sale to the purchaser. Similarly, the purchaser will often not record the purchaser's ownership of the mortgages or interests in mortgages under State recording statutes. These facts are irrelevant and the seller's retention of the mortgage documents and the purchaser's decision not to record do not change the trustee's obligation to turn the mortgages or interests in mortgages over to the purchaser. The application of section 541(d) to secondary mortgage market transactions will not be affected by the terms of the servicing agreement between the mortgage servicer and the purchaser of the mortgages. Under section 541(d), the trustee is required to recognize the purchaser's title to the mortgages or interest in mortgages and to turn this property over to the purchaser. It makes no difference whether the servicer and the purchaser characterize their relationship as one of trust, agency, or independent contractor.

The purpose of section 541(d) as applied to the secondary mortgage mar-

> ket is therefore to make certain that secondary mortgage market sales as they are currently structured are not subject to challenge by bankruptcy trustees and that purchasers of mortgages will be able to obtain the mortgages or interest in mortgages which they have purchased from trustees without the trustees asserting that a sale of mortgages is a loan from the purchaser to the seller.

From the legislative history, it is apparent that during drafting of § 541(d), Congress' sole concern was secondary mortgage market transactions. Hence, § 541(d) should be limited in application to that area. To hold otherwise would make § 541(d) redundant and mere surplusage. As Senator DeConcini stated:

> section 541(a)(1) clearly states, the estate is comprised of all legal or equitable interests of the debtor in property as of the commencement of the case. To the extent such an interest is limited in the hands of the debtor, it is equally limited in the hands of the estate except to the extent that defenses which are personal against the debtor are not effective against the estate.

124 Cong.Rec. 33,999 (1978).

In making the preceding determination, this court agrees with the majority of courts which hold that § 544(a) and § 541(d) operate independently, See, e.g., Cascade, 65 B.R. 35; Clark v. Kahn (In re Dlott), 43 B.R. 789 (Bankr. D.Mass.1983); Loup v. Great Plains Western Ranch Company, Inc. (In re Great Plains Western Ranch Company, Inc.), 38 B.R. 899 (Bankr. C.D.Cal.1984); McAllester v. Aldridge (In re Anderson), 30 B.R. 995 (Bankr. M.D.Tenn.1983); Elin v. Busche (In re Elin), 20 B.R. 1012 (Bankr. D.N.J.1982) aff'd. 707 F.2d 1400 (3rd Cir.1983), and disagrees with those cases which hold that § 541(d) is a general limitation on the trustee's powers under § 544(a). See, e.g., Vineyard v. McKenzie

(In re Quality Holstein Leasing), 752 F.2d 1009 (5th Cir. 1985); Cook v. United States (In re Earl Roggenbuck Farms, Inc.), 51 B.R. 913 (Bankr. E.D.Mich.1985).

This court found the history of the strong arm clause in In re Great Plains Western Ranch Co., Inc. to be especially enlightening. There the court observed:

> The trustee's powers under § 544(a), like his rights under Section 541, are derivative. But they derive from a different source. Under Section 541, his rights are derivative from the rights of the debtor. Under the predecessors of Section 544(a), his rights were derivative from the rights of creditors. The substance of this provision [Bankruptcy Act of 1898 § 70c] was carried over into the Bankruptcy Act of 1978. With respect to personal property, it makes sense to dovetail the rights of the trustee with the rights of creditors, because the most relevant state property law is in the Uniform Commerical Code, which builds its priority scheme primarily on the rights of creditors. But the law of real property is built around the recording acts. And recording acts frequently speak not of the rights of creditors, but rather of the rights of bona fide

> purchasers. Hence, the 1978 Code added a new provision to the strong-arm clause in Section 544(a)(3). It provides that the trustee shall have the powers of a hypothetical bona fide purchaser of real property. He is limited as a prospective bona fide purchaser would be limited. But he takes free of competing interests of which a bona fide purchaser would take free. The trustee exercises that power without regard to his own actual knowledge.

Great Plains, 38 B.R. at 905. (citations omitted).

The most recent case addressing the § 541(d)/§ 544(a) tension is that of City National Bank of Miami v. General Coffee Corp. (In re General Coffee Corp.), 828 F.2d 699 (11th Cir.1987) cert. denied, -- U.S. --, 108 S.Ct. 1470, 99 L.Ed.2d 699 (1988). There, the Eleventh Circuit was determining "whether an ideal creditor would prevail over a constructive trust beneficiary under Florida law." Id. at

706. The court resolved the issue by ruling "that for purposes of priority in bankruptcy a constructive trust beneficiary should have the same rights to the trust assets that a beneficiary of an express trust would have." Id. The court added that "[a]n express trust beneficiary clearly has priority to trust assets over a judicial lienholder or execution creditor." Id. (footnote omitted). Nevertheless, the court added that "a constructive trust beneficiary prevails over all subsequent takers of the trust property except bona fide purchasers."[12] Id. at 707. (citation omitted).

The plaintiffs' final contention is that the trustee cannot quality as a bona fide purchaser under § 544(a)(3) because he

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[12] This somewhat confusing decision maybe the result of General Coffee Corp. arguing that a constructive trust is essentially an equitable lien. However, the court rejected that

had constructive notice of their interests in the leasehold. In support of this position, the plaintiffs argue that the trustee was bound to inquire of Plunkett and/or the Pan-Am tenants regarding the tenants' interests in the property and the identities of the parties receiving rent. They submit that on inquiry Plunkett would have informed the trustee that the Pan-Am Pavilion Partnership owned the leasehold and that the tenants would have said that rental payments were "generally" made to the "Pan-Am Pavilion." (Reply Brief in Support of Plaintiffs' Motion for Summary Judgment at 4-5.)

Section 544(a)(3) makes a trustee's

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argument, stating that a constructive trust beneficiary has an equitable ownership interest. 828 F.2d at 706.

knowledge irrelevant, even though a trustee is subject to constructive notice as determined under state or other applicable law. See, e.g., Probasco v. Eads (In re Probasco), 839 F.2d 1352 (9th Cir.1988); McCannon v. Marston, 679 F.2d 13 (3rd Cir. 1982). In this case, St. Croix, U.S. Virgin Islands, is the situs of the property in question, thereby requiring examination of Virgin Islands' statutes to determine the rights of a bona fide purchaser.

The Virgin Islands' recording statute states that "[e]very conveyance of real property hereafter made within the Virgin Islands which is not filed for record shall be void against any subsequent innocent purchaser in good faith and for a valuable consideration of the same real

property, or any portion thereof, whose conveyance is first duly recorded." V.I. Code Ann. tit. 28, § 124 (1975). In summary, this statute provides that a purchaser for value who acquires real property and properly records that interest first, without actual or constructive knowledge of prior "secret", unrecorded interests, defeats the earlier unrecorded interests.

Similarly, the Uniform Partnership Act (U.P.A.), as enacted in the Virgin Islands provides that a bona fide purchaser for value who acquires real estate without knowledge of title defects prevails over partners whose interests are not of record. The pertinent statute states:

> Where title to real property is in the name of one or more but not all the partners, and the record does not disclose the right of the partnership, the partners in whose name the title stands may convey

> title to such property, but the partnership may recover such property if the partners' act does not bind the partnership under the provisions of subsection (a) of section 41 of this title, unless the purchaser or his assignee, is a holder for value, without knowledge.

V.I. Code Ann. tit. 26, § 42(c) (1962) (emphasis added). A person has "knowledge" under this section when he not only has actual knowledge, but also when he has knowledge of "other facts as in the circumstances shows bad faith." V.I. Code Ann. tit. 26, §2(a) (1962).

The plaintiffs apparently failed to perceive the significance of these statutes. First, § 42(c) of the U.P.A., apparently provides that a bona fide purchaser cuts off any possible constructive trust which might otherwise arise from a partner's misconduct. Secondly, the aforementioned Virgin Islands' statutes

speak in terms of innocent purchasers without actual knowledge of facts which in the circumstances shows bad faith. Yet, in the hypothetical sale addressed by § 544(a)(3), the trustee's actual knowledge is of no significance. The court will give no weight to plaintiffs contention that the trustee should have interrogated Plunkett and the Pan-Am tenants to determine whether there were "secret" interests in the leasehold.

The court finds also that the evidence does not support plaintiffs' constructive notice theory. The Pan-Am leasehold was acquired and recorded in Plunkett's individual name; all tenants occupied their premises pursuant to leases signed by Plunkett or his predecessor; and rent was paid to

Plunkett, Plunkett owned entities or accounts traceable to Plunkett. No one else was in possession of the proeprty and no one independent of Plunkett appeared to have an interest in the property. In fact, the evidence supports the trustee's view that tenants believed Plunkett was the sole owner of Pan-Am.

For the foregoing reasons, the plaintiffs' motion for summary judgment must be denied and the trustee's cross motion for summary judgment must be granted.[13]

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[13] Because the third-party defendants' claimed interests in the Pan-Am leasehold are avoidable by the trustee, they have no interests in the property to support their third-party set-off claim.

JUDGMENT--ORAL ARGUMENT

UNITED STATES COURT OF APPEALS

For the Seventh Circuit
Chicago, Illinois 60604

June 6, 1989.

Before

Hon. WILLIAM J. BAUER, Chief Judge
Hon. WALTER J. CUMMINGS, Circuit Judge
Hon. FRANK H. EASTERBROOK, Circuit Judge

No. 88-3189
IN THE MATTER OF:
OLIVER PLUNKETT and MONICA PLUNKETT Debtors,) Appeal from the United States District Court for the Eastern District of Wisconsin
APPEAL OF:
RAY J. BELISLE, et al., etc.) No. 88 C 655 Judge Myron L. Gordon

This case was heard on the record from the United States District Court for the Eastern District of Wisconsin, Division, and was argued by counsel.

On consideration whereof, IT IS ORDERED AND ADJUDGED by this Court that the judgment of the said District Court in this cause appealed from be, and the same is hereby, AFFIRMED, with costs, in accordance with the opinion of this Court filed this date.